Sankaty Advisors

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Dear Sankaty Credit Opportunities II Investor,

We are pleased to report that COPs II returned 32.2% gross and 28.9% net of all fees and expenses in 2009. As of year end, the NAV for COPs II had increased to 0.84x net on an estimated basis, well off its low of 0.63x last March. More importantly, relative to a year ago, we feel much more optimistic about the band of potential outcomes for the Fund given the stabilization of the economy and capital markets. The Fund has now completed its reinvestment period and should resume distributions in late 2010.

**Market Review**

While the 2009 market rally was broad based, how and when one deployed capital made the difference between solid and spectacular returns. The credit markets stabilized in 2009, and after a tough first quarter, the leveraged loan and high yield bond asset classes posted record returns. The "bottoming" of the economy provided an important fundamental catalyst as it enabled the market to identify winners and losers. Market technicals were strong throughout the year as investors plowed into credit from other asset classes, coupled with limited net new supply. What new issuance there was almost exclusively refinanced and extended existing debt, thus no new net supply was created.

Positive catalysts for the market included limited new issuance, the emergence of bond-for-loan take-outs, and reduced default expectations as riskier borrowers secured amend-to-extend loans and covenant relief. The return of some liquidity to the market improved access to capital, which led to a moderation in the current default rate.

As we see it, the market and economic data remains paradoxical. While recent WSJ articles have reported small businesses declining at record pace, economists point to small businesses as the critical driver of economic growth and employment. On the consumer side, spending continues its steady recovery, up 3.5% over the last twelve months returning to peak 2008 levels. However, in February, consumer confidence dropped sharply to its lowest level since April 2009 ($17^{th}$ percentile over the last 43 years). Further compounding the ambiguity of the current economic backdrop, recent reports indicate stabilizing housing prices, while others show new and existing home sales hitting all-time lows. On the macro side, markets continue to punish the Euro for the budget problems of some of its smallest economies, while they now favor the dollar in spite of the fact that some of the U.S.'s largest states face unprecedented budget shortfalls exacerbating record federal deficits.

What we do know is that these market dichotomies often lead to pockets of opportunity. In 2009, we found compelling investment opportunities created by a lack of DIP financing, a shortage of 2nd lien financing, and a general freeze on middle market lending. We highlight some of these investments below.

Given that the Fund has ended its reinvestment period, we will look to exit investments when price targets are met or when companies refinance our illiquid positions.

**Portfolio Review**

The Fund's liquid credit assets drove 2009 performance, returning over 80% gross for the year. In the fourth quarter, we sold over $100 million of securities in order to redeploy the proceeds across the core strategies. Notable 2009 winners include Manchester United and United Components. Manchester United rallied on the likelihood of a partial pay down through refinancing. United Components outperformed substantially, returning more than 450% in 2009, as the auto replacement part aftermarket benefitted from increasing mileage trends. We took advantage of the rebound in auto credits and rotated out of names which hit our targets, such as Allison Transmission and Accuride, in favor of adding new stressed and distressed positions, including Algoma Steel and Champion Home Builders. The table below highlights the Fund's 2009 outperformance of its benchmarks in both loans and bonds in the U.S. and Europe.

| 2009 COPs II Liquid Credit Performance | | | | |
|---|---|---|---|---|
| | Loans | | Bonds | |
| **US** | Returns | % Portfolio | Returns | % Portfolio |
| Sankaty | 71.9% | 21.1% | 102.6% | 47.4% |
| Index | 51.6% | | 58.9% | |
| **Europe** | | | | |
| Sankaty | 80.2% | 23.6% | 113.7% | 7.9% |
| Index | 48.5% | | 67.4% | |
| **Total** | | | | |
| Sankaty | 76.3% | 44.7% | 104.1% | 55.3% |

The Fund's structured investments returned over 8% gross for the year. Both the Race Point III and Nash Point CLO portfolios are in good shape as the high yield refinancing wave resulted in a number of pay downs. Nash Point has resumed making equity distributions, while Race Point III should begin to do so in 2010. We continue to believe the Fund's CLO holdings have significant upside remaining.

In our middle market portfolio, company performance has stabilized and our confidence in earnings forecasts has increased considerably. Cost cuts have produced higher than expected EBITDA levels given the sales declines we witnessed in 2009. Some of our early cyclical investments are starting to see a rebound in demand, while our consumer-facing businesses are still awaiting a recovery. Importantly, most of our companies are expecting improved results in

2010. In the case of Fieldbrook Farms, by foregoing a 2009 exit, the sponsor believes there is potential to earn another multiple or two following a strong year of stable operating performance. In addition, both Dawes and Transilwrap made small acquisitions in 2009 that should be highly accretive in 2010.

The Fund invested roughly $40 million in new middle market mezzanine deals in 2009. Our activity in this space is a result of the significant premium we see in less liquid and private opportunities. Moreover, our participation is diversified across industries and in terms of the financing role we play. For example, Sankaty recently helped finance Princeton Review's purchase of Penn Foster. Additionally, COPs II participated in two rescue financings of well-known retailers with strong collateral coverage that were looking for short-term liquidity to support restructuring initiatives. Lastly, we purchased senior subordinated notes and three classes of junior subordinated notes in Rug Doctor from a business development corporation looking to sell assets and reduce its leverage. Our first dollar out sits at 1.7x net leverage and expected IRRs of each tranche range from approximately 16% for the senior subordinated notes to 19% for the tranche C junior subordinated notes. The Rug Doctor is a well-run business that we have followed closely for years but had bid unsuccessfully to finance in the past.

**Outlook**

The Fund's reinvestment period ended in December, and our focus has now shifted to harvesting returns. As we exit investments, we will look to make a distribution in late 2010.

Attached is a snapshot of the current portfolio and our positioning. As always, we are available to discuss any of this information or answer any questions you may have. Please feel free to contact Kyle Betty (kbetty@sankaty.com) or Jeff Hawkins (jhawkins@sankaty.com) directly.

Sincerely,

Sankaty Advisors

**SANKATY CREDIT OPPORTUNITIES II, LP**
**STATISTICAL SUMMARY**
**(as of December 31, 2009)**

## STATISTICAL ANALYSIS* [1,2]

| | Q409 Gross Return | Q409 Net Return | 2009 Gross Return | 2009 Net Return | Annualized ITD Net Return | Sharpe Ratio |
|---|---|---|---|---|---|---|
| Sankaty Credit Ops II | 17.7% | 17.0% | 32.2% | 28.9% | -2.0% | (0.21) |
| S&P 500 (w/ dividends) | 6.0% | 6.0% | 26.5% | 26.5% | 0.6% | (0.04) |
| JPM HY Index | 6.3% | 6.3% | 58.9% | 58.9% | 7.5% | 0.40 |
| LSTA Loan Index | 3.8% | 3.8% | 51.6% | 51.6% | 4.7% | 0.21 |

* Net returns are net of all fees, expenses and carry.

## TOP ISSUERS [3]

**Top 10 Issuers (excluding Mezzanine & Structured)**

| Issuer | Fund Net Equity (%) |
|---|---|
| Manchester United | 3.1% |
| United Components | 2.9% |
| Applied Systems | 2.1% |
| ServiceMaster | 1.7% |
| Impress Group | 1.6% |
| Ariel | 1.5% |
| Rexnord | 1.4% |
| Dollarama | 1.4% |
| JW Aluminum | 1.4% |
| Dockwise | 1.2% |

**Top 5 Mezzanine Issuers**

| Issuer | Fund Net Equity (%) |
|---|---|
| Continental Cement | 2.4% |
| Restaurant Technologies | 2.4% |
| Dawes | 2.0% |
| Davis Petroleum Corp. | 2.1% |
| Fieldbrook Farms | 1.9% |

**Top 5 Structured Issuers**

| Issuer | Fund Net Equity (%) |
|---|---|
| Race Point III | 2.6% |
| Nash Point | 2.5% |
| Beach Street V | 2.4% |
| Chatham Light II | 1.9% |
| Sankaty II | 1.0% |

## FUND NET EQUITY ($m)

| | 09/30/09 | Profits | Net Contributions/ (Distributions) | 12/31/09 |
|---|---|---|---|---|
| Partners' Capital | $854.7 | $149.9 | $0.0 | $1,004.6 |

## BALANCE SHEET (MV in $m)

| | Long (A) | Short (B) | Net (A)-(B) | Gross (A)+(B) |
|---|---|---|---|---|
| Cash | $55.3 | $0.0 | $55.3 | $55.3 |
| Collateral (Restricted Cash) | 72.6 | 0.0 | 72.6 | 72.6 |
| | $127.9 | $0.0 | $127.9 | $127.9 |
| **By Asset Class** | | | | |
| Loans | $113.5 | $0.0 | $113.5 | $113.5 |
| Bonds | 223.2 | 0.0 | 223.2 | 223.2 |
| CDS/LCDS[3] | 19.7 | 6.0 | 13.7 | 25.7 |
| Mezzanine (Private Debt) | 363.0 | 0.0 | 363.0 | 363.0 |
| Equity (Public & Private) | 71.6 | 0.0 | 71.6 | 71.6 |
| Structured[3] | 191.8 | 0.0 | 191.8 | 191.8 |
| | $982.8 | $6.0 | $976.8 | $988.8 |
| **By Region** | | | | |
| North America | $834.8 | $4.1 | $830.7 | $838.9 |
| Europe | 148.0 | 1.9 | $146.1 | $149.9 |
| Other | 0.0 | 0.0 | $0.0 | $0.0 |
| | $982.8 | $6.0 | $976.8 | $988.8 |
| **By Industry** | | | | |
| Non-Industry Specific | $182.8 | $0.0 | $182.8 | $182.8 |
| Financial Intermediaries | 99.6 | 0.0 | 99.6 | $99.6 |
| Retailers (other than food/drug) | 82.8 | 0.0 | 82.8 | $82.8 |
| Automotive | 59.7 | 0.0 | 59.7 | $59.7 |
| Oil and Gas | 56.3 | 0.0 | 56.3 | $56.3 |
| Conglomerates | 49.8 | 0.0 | 49.8 | $49.8 |
| Healthcare | 45.7 | 0.0 | 45.7 | $45.7 |
| Food Products | 45.3 | 0.0 | 45.3 | $45.3 |
| Insurance | 35.4 | 0.0 | 35.4 | $35.4 |
| Business Equipment and Services | 32.2 | 0.0 | 32.2 | $32.2 |
| Other | 293.2 | 6.0 | 287.2 | $299.2 |
| | $982.8 | $6.0 | $976.8 | $988.8 |
| Exposure (% of Equity) | 97.8% | 0.6% | 97.2% | 98.4% |

1 Portfolio returns are computed based on the change in value during the period of a theoretical investment made at the beginning of the period. The change in value of a theoretical investment is measured by comparing the aggregate ending value of Limited Partners with the aggregate beginning value adjusted for cash flows related to capital contributions or withdrawals during the period. Returns are geometrically linked on a monthly basis. Investment performance results depict the return of the Limited Partners of the Partnership as a whole. Returns of individual Limited Partners may differ based on the timing of contribution to or withdrawal from the Partnership. Investment performance reflects the reinvestment of profits, dividends and income. Net returns are stated net of all fees, expenses and carry (see footnote 2). Returns are estimated as of December 31, 2009 and are stated before the finalization of annual financial statements. As with all unaudited estimates, these estimates are subject to uncertainties and variations and may not be predictive of final results once audited. Actual outcomes and results may differ materially from the returns indicated herein.

2 Generally, the General Partner is entitled at year-end to a carry allocation equal to 20% of Net Profits for such fiscal year as discussed in the Limited Partnership Agreement. For purposes of presentation herein, the carry allocation has been included as a periodic expense and has been calculated on the Net Profits for the period. The Management Fee is a quarterly fee paid to Sankaty Advisors, LLC generally equal to 2% of each Limited Partner's capital account at the beginning of each quarter.

3 Single name CDS/LCDS, Index CDX/LCDX, Tranche CDX/LCDX, Structured CDS and Structured Revolvers included at maximum loss amount.